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Dianne Wampler 01/29/2007 12:20:14 PM From DB/Inbox: Dianne Wampler

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UNCLAS SENSITIVE ANKARA 00160

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INFO: CONS PA RAO FAS MGT PMA FCS POL DCM AMB

DISSEMINATION: ECON /1
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UNCLAS SECTION 01 OF 02 ANKARA 000160

SIPDIS

SENSITIVE

E.O. 12958: N/A
TAGS: [EINV](#) [BEXP](#) [PGOV](#) [TU](#)
SUBJECT: ECONOMIC FREEDOM IN TURKEY: MORE, BUT NOT ENOUGH

REF: ANKARA 38, B) 2006 ANKARA 6734

SENSITIVE BUT UNCLASSIFIED.

¶1. (SBU) Summary. According to the Heritage Foundation's 2007 Index of Economic Freedom (IEF), Turkey has made impressive strides in reducing the dead weight of government interference in the economy and economic decision-making over the past five years. This helps explain Turkey's similarly impressive investment performance, including large increases in FDI inflows, over the same period, along with the concomitant absence of new greenfield FDI (ref b). Although Turkey is one of fastest risers of the 157 countries included in the IEF, it still remains in the middle of the global pack in 83rd place. Deeper reforms are needed in order to sustain a competitive investment environment, particularly in a judicial system perceived as inefficient, corrupt, and biased. Such reforms require strong political will, underlining the importance of Turkey coming out of this election year with a government able to implement tough reforms. End Summary.

ABSOLUTE AND RELATIVE IMPROVEMENT

¶2. (SBU) Turkey's IEF ranking has dramatically improved in absolute and relative terms over the past 5 years. According to the Heritage Foundation's annual report, Turkey's 2007 score on 10 indicators of "economic freedom" averaged 59.3 out of a possible 100 points, placing it 83rd out of 157 countries scored. This compares to a score of 50.9 and 120th place in 2003. Turkey bottomed out in 2005 at 50.6, when it was in 124th place. The performance of only three countries -- Georgia, Romania, and Kazakhstan -- exceeded this 41 place improvement in Turkey's rank in just two years.

¶3. (SBU) Turkey's score improved in seven of the index's ten components. The most dramatic contributions to the higher overall score are in increased regulatory and financial freedom and in

monetary policy. Freedom from excessive government, trade openness, fiscal policy, and corruption scores also improved, but less dramatically. Scores for investment and property rights remained flat, while labor policies declined slightly. Although the IEF tries to minimize data discontinuities, some of the improvement also seems to result from better methodology. For example, the use of the World Bank's "Doing Business" database to measure regulatory freedom starting in 2006 seems to explain the sharp improvement in that indicator.

----- STUCK IN THE MIDDLE OF THE GLOBAL PACK -----

14. (SBU) Nonetheless, from the bottom 20% of countries ranked, Turkey has moved to the middle of the global pack. This is a vast improvement, but Turkey still has a long, long way to go to reach the levels of fast growing countries in Asia. Several countries with which Turkey competes for foreign investment, including Hungary, South Africa, Mexico, Brazil, and the Czech and Slovak Republics, rank higher, although some others, notably Poland, Greece, India, China and Russia, are lower (Table II).

----- Judicial Reform is Key -----

15. (SBU) To raise Turkey's overall rating, improvements are needed in all areas. Some of these will come more easily than others. For example, the monetary policy indicator is a simple average of inflation rates over the previous five years. But making progress on the other indicators will require structural reforms that are politically difficult. Turkey has the furthest to go to improve its corruption rating, which is imported from Transparency International's "Corruption Perceptions Index." Among other things, this will require improving the administration of justice and training a new generation of judges, in an environment in which changing the judiciary is a political hot button for Kemalist secularists. Other examples of how judicial and legal deficiencies affect Turkey's overall ranking are low scores for protection of property rights (including intellectual property) and freedom to invest, especially in real estate. Improving the labor law will require freeing up rigid labor laws, including severe legal limitations on companies' ability to lay off workers that are similarly sensitive politically.

----- Comment -----

16. (SBU) The improvement in economic freedom in Turkey over the past five years is impressive given where Turkey has come from. But there is still a lot to do. Although it may have some methodological shortcomings that make it slow to reflect on the ground improvements, the IEF is a useful reminder to the Turkish government of the need to focus reform efforts on the judicial system. Without this Turkey will not be able to sustain the high levels of foreign and domestic investment needed to per capita income from the current \$5,000 to European standards. This is another reminder (ref a) of the issues at stake in this election year and the importance of coming out of it with a government that has the broad-based support needed to implement deep reforms.

Table I
Index of Economic Freedom: Turkey

	2007	2006	2005	2004	2003	2002
Regulation	67.4	65.9	30	30	30	30
Trade	76.0	76.0	71.0	69.2	68.6	74.6
Fiscal	79.4	78.7	76.9	73.8	76.4	76.8
Government	69.9	72.7	62.3	64.6	53.9	66.8
Monetary	70.2	64.7	53.8	46.1	42.9	41.0
Investment	50	50	50	50	50	50
Financial	50	50	30	50	50	50
Property Rights	50	50	50	50	50	50
Corruption	35.0	32.0	31.0	32.0	36.0	38.0
Labor	45.4	44.6	47.6	-	-	-

Score	59.3	58.5	50.6	51.7	50.9	53.0
Rank	83	92	124	116	120	106

Table II
Country Comparisons

Country	2007 Rank	2007 Score
Cyprus	20	73.1
Czech Republic	31	69.7
Israel	37	68.4
Slovak Republic	40	68.4
Hungary	44	66.2
Mexico	49	65.8
South Africa	52	64.1
Jordan	53	64.0
Bulgaria	62	62.2
Romania	67	61.3
Brazil	70	60.9
Turkey	83	59.3
Poland	87	58.8
Greece	94	57.6
India	104	55.6
China, PR	119	54.0
Russia	120	54.0
Ukraine	125	53.3
Vietnam	138	50.0
Wilson		